Joint Legislative Audit Committee

OFFICE OF THE AUDITOR GENERAL

California Legislature

MIKE CULLEN
CHAIRMAN

December 29, 1977

Letter Report 711

The Honorable Speaker of the Assembly
The Honorable President pro Tempore of the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members of the Legislature:

This report is submitted in accordance with Section 41365 of the Health and Safety Code of the State of California. This section requires the Joint Legislative Audit Committee to report on the activities of the California Housing Finance Agency (CHFA) within 90 days following receipt of the Agency's annual report.

This report is based primarily upon the Joint Legislative Audit Committee's examination and evaluation of the Agency's annual report. The financial statements of the CHFA were examined by an independent certified public accounting firm which expressed an unqualified opinion on the fairness of the statements. In May 1977 three legislative committees held a joint hearing to review the Agency's activities. The State Department of Finance is completing an audit of CHFA compliance with state administrative procedures. The Joint Legislative Budget Committee plans to report on the Agency's activities and comment on CHFA's proposed 1978-79 budget prior to its adoption.

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Background

The California Housing Finance Agency was created by the Zenovich–Moscone–Chacon Housing and Home Finance Act of 1975 to meet the housing needs of persons and families of low or moderate income. To accomplish this, the Agency borrows money in the municipal bond market and is empowered to operate a wide variety of programs of lending and insuring mortgages and loans to make them available at lower-than-market interest rates.

The substance of the Agency is its ability to borrow money at favorable interest rates. This is made possible by the tax exempt status of interest paid on money borrowed. The Agency is authorized to issue bonds in the aggregate amount of $450 million.* The entire $450 million may be in tax-exempt revenue bonds not guaranteed by the Federal Government; or, $150 million of this amount may be in taxable revenue bonds guaranteed by the Federal Government.

The Agency's annual budget is established by the Agency's Board of Directors. The Agency was started with loans and capital contributions made available by the Legislature, however, it is intended that the Agency will repay the loans and function without appropriation. The Agency is to use the difference between the cost at which it borrows money and the rate at which it lends money to finance its operations and to repay the start-up loans.

Agency Operations 1976-77

The CHFA encountered two major impediments during the year.

- In August 1976, the Supreme Court determined that the Agency's direct lending activities for multi-unit projects constituted the "development of low cost public housing." Therefore, the direct lending activities for multi-unit projects are subject to local referendum as required by Article XXXIV of the State Constitution. The U. S. Department of Housing and Urban Development (HUD) reacted by reducing the HUD Section 8 (rent subsidy) funds set aside for CHFA by 30 percent and refusing to process most other project commitments outstanding after the Supreme Court decision. This caused a delay and a reduction in program scope.

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* A footnote to the CHFA June 30, 1977, financial statements reports that the Agency is authorized to issue bonds in the aggregate amount of $950 million. However, the Housing Finance Bond Law of 1976, authorizing the issuance of $500 million general obligation bonds subject to adoption by the electors was rejected at the general election held November 2, 1976, leaving authorization for only $450 million in revenue bonds.

The Agency reports that the Supreme Court decision creates a number of problems in attempts to meet legislatively mandated objectives while using HUD rental subsidies. However, the Agency claims it is attempting to optimize use of the HUD rental subsidies available. The Agency is also filing a lawsuit with the State Supreme Court pursuant to Chapter 1339, Statutes of 1976 which contained amendments designed to clarify certain constitutional provisions. If this suit is successful, the Agency would be able to finance mixed income rental housing developed by private sponsors without Article XXXIV approval.

- In the November 1976 general election, Proposition One was defeated. This proposition, if approved, would have authorized $500 million of state general obligation bond authority for use by the Agency.

  Legislation calling for a general obligation bond referendum is being considered by the Legislature. If approved by the Governor, this would again place the issue on the ballot.

The Agency's achievements during the year are small in comparison to California's total housing market. However, (1) CHFA programs are designed to service a narrow market, and (2) 1976-77 was the Agency's first full year of operation.

Multi-Unit Direct Lending Program

The Agency's financial statements and accompanying notes report that as of June 30, 1977, the Agency had purchased construction loans of $1 million and had commitments outstanding for the Multi-Unit Direct Lending Program for $30,600,000. Funds were provided by note sales of $15 million on January 25, 1977 and $16.6 million on March 29, 1977.

"Outstanding commitments" reported in the Agency's comment section of the annual report differ from "outstanding commitments" reported in notes accompanying the financial statements. The Agency's comment section reports outstanding commitments of over $47 million (approximately 1,600 units) which include conditional commitments assuming funds are obtained.

Mortgage Purchase Program

As of June 30, 1977, the Agency had purchased mortgage loans of $19.3 million and had outstanding commitments to purchase mortgage loans of $71.2 million for the Mortgage Purchase Program. This was the net amount available from the Agency's bond sale prior to June 30, 1977.

In October 1976, $100 million of FHA/VA tax-exempt mortgage purchase bonds rated AA were sold in a negotiated underwriting. The Agency obtained the money for varying periods extending up to 31 years, at a net average interest rate of 5.98 percent. Bond proceeds established required reserves and provided $90.5 million for the purchase of eligible mortgages.

The Agency reports that by June 30, 1977, 1,142 loans totaling $35.7 million were delivered to the Agency. In relation to the population distribution, a disproportionately large number of the 1,142 loans delivered to the Agency were from Sacramento County. The Agency reports 425 loans from Sacramento County, compared to only 24 loans from Los Angeles County, 8 loans from Orange County and no loans from San Francisco County. The Agency reports that loan originations tended to mirror the State's housing market conditions. Few loans were generated from high priced market areas. The program has FHA sales price and loan limits and CHFA income and asset limits.

Neighborhood Preservation

Neighborhood Preservation activities were under development and not yet operational during fiscal year 1976-77. With the proceeds from the sale of $25 million of home ownership and home improvement bonds on December 6, 1977, the Agency expects that a variety of financing activities will be made available, including rehabilitation, home improvement and home purchase loans. The available financing will coincide with Neighborhood Preservation area designations and with the implementation of the Rehabilitation Loan Insurance Program.

The Agency also plans to initiate a program to insure revenue bonds issued by local agencies pursuant to the Foran-Marks Residential Rehabilitation Act of 1973.

State Appropriations and Loans

The CHFA has received several state appropriations and loans.

California Housing Finance Fund

The California Housing Finance Fund received an advance of $10,750,000 from the State General Fund in September 1975. Of this amount, $10 million was designated for the Supplementary Bond Security Account and $750,000 for the Operating Account.

The $10 million remained in the Supplementary Bond Security Account at June 30, 1977, to be used as security for the issuance of revenue bonds. No transfers from the account were required during fiscal year 1976-77 to supplement bond reserve funds.

The statutes provide that the $10 million is to be repaid to the State General Fund when all obligations secured by the account are retired. Interest earned from investing the $10 million is to be paid annually to the General Fund.

The Operating Account received an advance of $750,000 in 1975 to pay the initial operating expenses of the Agency. The $750,000 advance is to be repaid without interest to the State General Fund on January 1, 1986 .

The Agency has not provided a reserve accumulation schedule for repayment of the advance to the Operating Account. However, for the year ended June 30, 1977, Operating Account revenues exceeded expenses by $469,031. This eliminated an Operating Account deficit of $336,738 at the beginning of the fiscal year and provided a fund balance of $132,293 at year end.

Housing Rehabilitation Insurance Fund

The Housing Rehabilitation Insurance Fund received a State General Fund advance of $5 million in September 1975. This advance was to provide reserves and to pay expenses of the Rehabilitation Loan Insurance Program. This advance, classified as a loan, is also to be repaid without interest by January 1, 1986.

The Housing Rehabilitation Insurance Fund also received a $5 million appropriation from the General Fund as of January 1, 1977. This appropriation, classified as fund balance, does not have to be repaid.

Expenses of the Housing Rehabilitation Insurance Fund for fiscal year 1976-77 exceeded revenues by $150,228. This resulted in an ending fund balance, including the $5 million appropriation from the State, of $4,956,491. The Agency advises that funding to restore the $5 million contributed by the State is to be derived from other agency revenues and income. The Agency intends to maintain the $5 million contribution to be used only if insurance losses exceed insurance income.

The Housing Rehabilitation Loan Insurance Program is not yet in operation. On-going funding for the program is to be derived principally from loan insurance premiums and investment income.

Respectfully submitted,

MIKE CULLEN
Chairman